

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08

EA-12 FRB-01 INR-10 IO-14 NEA-10 NSAE-00 ICA-20

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FM AMEMBASSY BONN

TO SECSTATE WASHDC 7911

DEPARTMENT TREASURY

INFO AMEMBASSY BRUSSELS

AMEMBASSY LONDON

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

USMISSION USBERLIN

USMISSION USNATO

AMCONSUL FRANKFURT

AMCONSUL MUNICH

AMCONSUL DUSSELDORF

AMCONSUL BREMEN

AMCONSUL HAMBURG

AMCONSUL STUTTGART

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USEEC, USOECD ALSO FOR EMBASSY

DEPARTMENT PASS FRB AND CEA

E.O. 11652: N/A

TAGS: ECON, EFIN, GW

SUBJECT: ECONOMIC RESEARCH INSTITUTE (DIW)

NOTES DIM MEDIUM-TERM PROSPECTS

-- URGES STIMULATION

1. THE GERMAN ECONOMIC RESEARCH INSTITUTE IN BERLIN

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(DIW) HAS JUST PUBLISHED A STUDY PAINTING A DIM PICTURE
OF MEDIUM-TERM GROWTH AND EMPLOYMENT PROSPECTS IN THE
FRG AND URGING ADDITIONAL AND SUSTAINED PUMP-
PRIMING. ASSUMING NO FURTHER FISCAL STIMULATION, DIW
CALCULATES THAT REAL GROWTH THROUGH 1985 IS NOT
LIKELY TO EXCEED AN AVERAGE ANNUAL RATE OF 2.5
PERCENT; BY 1985, SOME 2.6 MILLION PEOPLE WOULD BE

SEEKING A JOB AND OFFICIALLY REGISTERED UNEMPLOYMENT
WOULD COME TO ABOUT 2 MILLION.

2. AGAINST THIS BACKGROUND, DIW URGES A HIGHER LEVEL OF
PUBLIC SECTOR EXPENDITURES, PARTICULARLY FOR INFRA-
STRUCTURE AND PROMOTION OF HOUSING CONSTRUCTION, BUT
ALSO FOR GOVERNMENT CONSUMPTION -- PRINCIPALLY THROUGH
INCREASED PUBLIC SECTOR EMPLOYMENT. DIW RECOMMENDS
THAT ANTICIPATED OUTLAYS THROUGH 1985 BE RAISED BY
AT LEAST DM 130 BILLION (1970-PRICES). THIS, THE DIW
CALCULATES, WOULD HAVE MULTIPLIER AND ACCELERATOR
EFFECTS ON PRIVATE SECTOR DEMAND OF DM 250 BILLION
(1970-PRICES). DIW CONCLUDES THAT AN ADDITIONAL 1.9
MILLION JOBS WOULD BE CREATED BY 1985 AND ANNUAL REAL
GROWTH DURING THIS PERIOD WOULD BE RAISED TO 3.4
PERCENT.

3. FOLLOWING BELOW IS A TABLE SUMMARIZING THE IMPACT
OF THE PROPOSED PROGRAM ON THE DEVELOPMENT OF GNP
AND ITS COMPONENTS, AS ESTIMATED BY DIW.

DIW ESTIMATES OF FRG GNP

CONSTANT - 1970 - PRICES

1978 - 1985 1985

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AVERAGE ANNUAL PERCENT
CHANGE FROM PREVIOUS

YEAR'S LEVEL BILLION DM

ASSUMING ASSUMING
IMPLEMENT- IMPLEMENT-
ATION OF ATION OF

STATUS QUO PROPOSED STATUS QUO PROPOSED
PROJECTION PROGRAM PROJECTION PROGRAM

PRIVATE

CONSUMPTION 2.4 3.0 548 573

GOVERNMENT

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CONSUMPTION 2.0 2.7 167 177
FIXED
INVESTMENT:
BUSINESS 3.0 6.1 134 169
HOUSING 0.5 3.1 46 56
GOVERN. 2.5 5.6 35 45
CHANGE IN
INVENTORIES -- -- 10 12
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NET FOREIGN
BALANCE -- -- 40 20
EXPORTS 4.0 4.0 303 303
IMPORTS 3.8 4.8 263 283

GROSS -----
DOMESTIC
PRODUCT 2.5 3.4 980 L,052

4. ACCORDING TO DIW, THE CURRENT COSTS OF THE PROGRAM -
COME 1985 - WILL BE OVERCOMPENSATED BY CURRENT SAVINGS
ON TRASFER PAYMENTS (UNEMPLOYMENT BENEFITS, SOCIAL
WELFARE) AND STEPPED-UP RECEIPTS FROM TAXES AND SOCIAL
SECURITY PREMIUMS. IN CALCULATING THE LATTER, THE
INSTITUTE ASSUMED AN UNCHANGED RATIO OF TAXES AND OF
SOCIAL SECURITY CONTRIBUTIONS TO GNP. THIS CLEARLY
SUGGESTS THAT IT IS INCREASED DEFICIT SPENDING, NOT
TAX INCREASES, THAT THE INSTITUTE HAS IN MIND FOR FIN-
ANCING THE EARLIER PHASES OF ITS PROGRAM, I.E., UNTIL
RECEIPTS HAVE CAUGHT UP WITH OUTLAYS.

5. COMMENT -- THE DIW PRESCRIPTION RELIES HEAVILY ON
THE ASSUMPTION THAT THERE IS A LARGE UNFULFILLED DEMAND
FOR PUBLIC GOODS WHICH, IF AND WHEN MET, WOULD GIVE A
BOOST ALSO TO THE PRIVATE SECTOR. THIS IS NOT A VIEW
SHARED WIDELY BY KNOWLEDGEABLE OBSERVERS OF THE GERMAN
ECONOMIC SCENE, EITHER INSIDE OR OUTSIDE THE GOVERNMENT.
MOST WOULD ALSO QUESTION THE DIW'S ASSUMPTION THAT LACK
OF DEMAND IS THE PRINCIPAL EXPLANATION FOR GERMAN
UNEMPLOYMENT. NOTEWORTHY IN DIW'S PROPOSED
PROGRAM PROGNOSIS IS THE SHARP DECLINE IN THE NET
FOREIGN BALANCE. THIS WOULD BE WELCOMED BY THOSE
WHO SEE CURRENTLY TOO GREAT A DEPENDENCE ON THE FOREIGN
SECTOR AS WELL AS THOSE OPPOSED TO LARGE PRIVATE
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SECTOR RESOURCE TRANSFERS ABROAD.
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